KENTUCKY FRIED CHICKEN CORPORATION 1970 ANNUAL REPORT

Kentucky Fried Chicken Corporation's International Headquarters, dedicated near the end of fiscal 1970, stands as more than a symbol of a company that has grown in six years from a business headquartered in Colonel Harland Sanders' back yard in Shelbyville, Kentucky, to the world's largest commercial food service operation. The structure symbolizes a company which has come of age. While it captures the charm of the South so closely identified with The Colonel and his product, the building has been especially designed for functional efficiency, from the climate-controlled data processing center and the food research and test kitchen which occupy the lower level to the 173 separate offices on the upper three levels which house executive, administrative and operations personnel. Occupancy of the new 88,000 square foot headquarters in mid-July marked the first time the company has been housed in quarters designed for its specific needs; needs which have grown more critical with the rapid growth of the company. In the new International Headquarters, Kentucky Fried Chicken Corporation has the functional control center necessary to meet the demands of continued growth in the years ahead.

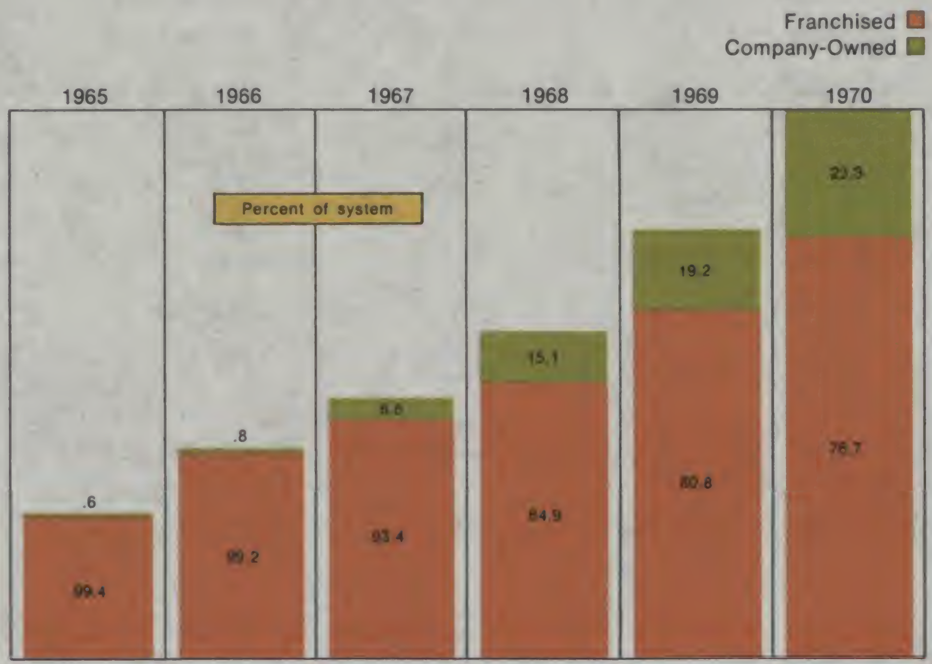
KFC International Headquarters Dedicated September 16, 1970
Cover Illustration

FINANCIAL HIGHLIGHTS

Years ended September 30	1970	*1969	*1968	*1967	*1966 (Unaudited)	*1965 (Unaudited)
Gross Income	$205,972,269	$163,826,880	$112,354,626	$67,311,535	$48,867,902	$31,780,570
Income Before Taxes and Extraordinary Items	27,489,676	26,917,536	16,658,230	7,865,731	5,850,307	2,825,203
Taxes on Income	14,521,000	14,038,000	8,449,000	4,040,685	2,932,661	1,304,518
Net Income	13,251,961(a)	12,879,536	8,209,230	3,825,046	2,917,646	1,520,685
Net Income Per Share	1.27(a)	1.24	.81	.39	.31	.18
Average Number of Shares Outstanding**	10,466,431	10,351,151	10,170,000	9,787,611	9,314,471	8,642,552

*Restated to reflect the elimination of the minority interest in the Kentucky corporation.
**Restated to reflect increase in shares contingently issuable under certain acquisition agreements.
(a) Includes $283,285 or $0.03 per share attributable to income from extraordinary items.

DOMESTIC OUTLETS IN OPERATION



FOREIGN AND DOMESTIC OUTLETS IN OPERATION

	Year Ended September 30	
Kentucky Fried Chicken	**1969**	**1970**
Franchised	1,907	**2,315**
Company-owned	481	**625**
H. Salt, esq., English Fish & Chips		
Franchised	109	**204**
Company-owned	2	**145**
Kentucky Roast Beef		
Franchised	64	**58**
Company-owned	6	**53**
Total		
Franchised	2,080	**2,577**
Company-owned	489	**823**
Grand Total	2,569	**3,400**

TO OUR SHAREHOLDERS

Kentucky Fried Chicken Corporation achieved in fiscal 1970 its objectives of building organizational strength and the food service distribution network necessary to advance its position of industry leadership established during an unprecedented expansion in the 1960s.

The gross revenue and net income of your Company during fiscal 1970 reflect prevailing economic conditions as well as a considerable investment in the development of international operations and the H. Salt, esq., English Fish & Chips program. These programs did not contribute significantly to 1970 earnings, but we believe our future growth has been enhanced by the decision to invest a portion of this year's profits in the long-term opportunity of the international market and the new fish & chips field.

Sales and operating income totaled $205,972,269, as compared with $163,826,880 in fiscal 1969. Net income totaled $13,251,961, or $1.27 per share, as compared with the restated $12,879,536, or $1.24 per share, in 1969.

These figures represent further growth during a period in which profits of many companies, including most in our own industry, were severely restricted by national economic conditions. While results of fiscal 1970 are not unfavorable, especially in light of the essential investments already noted, they did not equal the dramatic growth of previous years. Nor do they represent an acceptable pattern for future growth.

We are pleased to report that this year we exceeded our previously stated objective of 750 new outlets with the opening of 831 new domestic and international outlets by the Company and its franchisees. Growth during 1970 brings total units of all types to 3,400 at fiscal year end, including 2,940 Kentucky Fried Chicken stores, 349 H. Salt, esq., English Fish & Chips shoppes, and 111 Kentucky Roast Beef outlets.

The Company has continued to emphasize Company-owned operations, which now produce approximately one-half of our corporate profits. More new Company-owned outlets were built during fiscal 1970 than during all previous years combined. At the end of fiscal 1970, the Company owned and operated 823 food service outlets of all types. We chose not to pursue an aggressive franchisee acquisition program in 1970 while consolidating our rapid gains of past years. We feel your Company is now prepared to proceed with acquisition opportunities in selected market areas during 1971.

The H. Salt, esq., English Fish & Chips program, which we consider the most promising new fast food concept, was virtually tripled in size during fiscal 1970 to establish a position of significant market leadership. As might be expected of a new program, start-up costs have been substantial in relation to returns, and the program's mixed pattern of sales during its relatively short history presently does not permit solid projections of its future contribution to corporate earnings. We are confident that continuing efforts will determine the most profitable method of sales and distribution for this young program.

A slight decline in Kentucky Fried Chicken unit sales volume accompanied the restricted economic conditions of fiscal 1970. This pattern appeared early in the second quarter and stabilized shortly thereafter. We anticipate that new menu combinations, the introduction of new products, and a general improvement in the economy will increase unit volume. Preliminary market tests of certain new products for

existing outlets show considerable promise, but it is too early to determine their contribution to future sales. While we are concentrating on increasing per unit volume, our long term objective is total market penetration and profit opportunity as it relates to our return on investment.

The Company initiated during 1970 programs offering the potential for continued vital growth. Present franchisees are participating in our program of expansion into a sizable number of communities of 5,000 to 15,000. For this purpose, a broader menu and specially designed building and equipment package have been developed. Another program will develop secondary locations in existing metropolitan markets, and a third provides for continuing expansion in previously undeveloped metropolitan markets. Included in the latter category is New York City, where the initial Kentucky Fried Chicken stores are producing the highest unit sales volumes within our system.

Your Company achieved its stated objective of building organizational depth during 1970 in order to realize maximum corporate growth from the opportunities of this new decade. This objective was based on acknowledgment that the organization which built Kentucky Fried Chicken Corporation from a $7 million company to a $200 million company in five years must be broadened to consolidate past gains and to capitalize on the advantages inherent in our industry leadership.

This management organization has arranged substantial financing and developed improved fiscal controls, field accounting, computerized reporting and cost controls. It also is developing marketing techniques and programs to utilize the nation's largest fast food distribution network to its fullest potential. Objectives of these programs include the development of new products, improved marketing of existing products, more efficient and economical building and equipment packages, increased operational efficiency, and increased unit sales volume.

Your management has chosen to forego, for the present, further development of the Colonel Sanders' Inns program. The Company presently owns motels in Houston and Oklahoma City, as well as a new Louisville facility to be ready for occupancy in early 1971. Our entry into this field was based on the belief that it was a logical extension of our service-oriented Company. The drastic change in availability of financing for such programs has prompted reassessment of priorities, and we have chosen to concentrate on the food service industry's greater growth potential and profitability.

Test marketing of a new concept and new menu, featuring steak and a high quality hamburger, is underway to find the best means to generate satisfactory returns in the Kentucky Roast Beef program, which was not expanded during fiscal 1970. Further development of the program will depend upon the success of these tests.

Fiscal 1970 was a year in which our industry faced its greatest test in the consumer marketplace. Many companies not established on sound concepts were found wanting, but the test served to strengthen the position of proven industry leaders. Your Company has emerged in a greater position of leadership, and will continue to pursue growth-oriented policies through which this margin of leadership can be expanded.

Your Company's successful growth is a tribute to products of unequalled high quality which offer a full, wholesome take-home meal at a moderate price and to the trend of urban life which demands such conveniences. This trend, with its increasing mobility, increasing affluence and increasing freedom from the kitchen and the home is expected to accelerate in the years ahead.

Kentucky Fried Chicken Corporation is built on innovation — the innovation which led Colonel Sanders to develop his unique product, the innovation which motivated Haddon Salt to introduce his successful English product to the American appetite, and the innovation which introduced take-home service and a successful franchising concept to the food service industry during the past decade. As the leader in its field, your Company is dedicated to this continued innovation in building a new decade of growth during the 1970s.

John Y. Brown, Jr.

John Y Brown Jr

President, Chairman of the Board and
Chief Executive Officer

Richard C. Beeson
Executive Vice President
Chief Operating Officer

CORPORATE OPERATIONS

Innovation in the development of new marketing techniques, new products, and new markets continued to be the theme of corporate planning during fiscal 1970. Primary corporate objectives continue to be expansion of leadership in the food service industry, increased growth through further development of proven, profit-generating concepts, extension of Company-owned operations, the introduction of new concepts and new products, and the further development of programs of exceptional potential.

Kentucky Fried Chicken Corporation reappraised its overall position and strategies during the year by talking to consumers, analyzing the market place, researching the food service competition profile and reviewing the corporation's own structure to a greater degree than ever before. These studies have provided more definitive information upon which to base plans and decisions in all phases of the business. Comprehensive management policies were implemented to establish a broader personnel base, designed to position the Company for maximum market penetration and profit realization.

An intensified management development and training program, with emphasis on management by objectives and appraisal of achievement, was initiated during the year. This program is expected to add a new dimension to Kentucky Fried Chicken personnel policy. KFC personnel will continue to stress quality of product, courtesy and speed of customer service, imaginative merchandising and advertising, as well as responsible management.

During the year Company operations were expanded to a total of 823 units, including 606 Kentucky Fried Chicken stores. About half of the Company's net income is now being generated by these Company-owned stores. More than 20 per cent of all Kentucky Fried Chicken stores and more than 40 per cent of all H. Salt, esq., English Fish & Chips shoppes are Company-owned.

In addition to providing an expanding revenue base, these stores pioneer market testing of new products and new marketing, advertising and promotional techniques. While successful programs are passed on to franchisees, the expense

of all major field testing and research programs is borne by the Company.

Consumer and market testing to determine consumer acceptance of new concepts and products is continuing. An extended menu which offers more combinations of standard items has been introduced in some test areas. Numerous other new product ideas are in the field for further evaluation.

The H. Salt, esq., English Fish & Chips program was aggressively expanded during fiscal 1970. While this operation is in early development stages, the opening of 238 new H. Salt outlets during fiscal 1970 establishes a position of leadership in this new fast food field.

In addition to the continued development of new franchised and Company-owned stores in the many traditional markets which remain for Kentucky Fried Chicken, the Company has developed broader menu programs, as well as building and equipment packages, especially suited to promising secondary locations in existing prime market areas and to communities of 5,000 to 15,000 population. Both a modular building and a "mini-building" have been developed for these market areas. The building packages designed for smaller communities are suited to H. Salt, esq., English Fish & Chips shoppes as well as Kentucky Fried Chicken stores.

At the end of fiscal 1970, franchised and Company-owned outlets selling products of Kentucky Fried Chicken Corporation in the United States and abroad totaled 3,400, including 2,577 franchised and 823 Company-owned units.

Robert S. Barlow
Group Vice President
Operations

Joseph I. Kesselman
Group Vice President
Finance and Administration

FINANCE AND ADMINISTRATION

Fiscal 1970 was a year of solid progress in the area of finance and serves as the basis of continued improvement in the Company's utilization of its financial resources.

It is gratifying that during a period of tight money your Company was able to negotiate non-equity financing of $50 million from a group of prominent banks. These funds enable KFC to improve its liquidity and permit the orderly disposition of real estate and equipment on a sale-leaseback basis, a program which frees funds for more productive uses.

Development of a more efficient and more economical accounting system and the establishment of regional accounting centers during the year was undertaken to provide management with more detailed and timely management and financial reports. With these improvements, the Company can better detect and deal promptly with developments which appear inconsistent with corporate objectives. More sophisticated programs currently being developed will enable the Company to improve its cash flow from the field, expedite collection of accounts receivable and provide automated handling of billing and inventory controls.

The Consolidated Financial Statements which follow are based upon conservative accounting principles which Kentucky Fried Chicken Corporation has consistently employed, and which now are being widely adopted throughout our industry.

KENTUCKY FRIED CHICKEN CORPORATION 1970 ANNUAL REPORT

CONSOLIDATED FINANCIAL STATEMENTS

STATEMENT OF CONSOLIDATED OPERATIONS

Kentucky Fried Chicken Corporation
and Consolidated Subsidiaries

	Year Ended September 30	
	1970	**1969—Note A**
Net sales	**$192,778,618**	$153,496,291
Monthly franchise fees—Note B	**10,865,606**	7,661,923
Initial franchise fees	**1,379,698**	1,970,195
Other operating income	**948,347**	698,471
	205,972,269	163,826,880
Costs and expenses:		
Cost of goods sold	**105,401,550**	79,283,998
Selling, general, and administrative expenses	**70,907,931**	56,895,131
	176,309,481	136,179,129
	29,662,788	27,647,751
Other income	**1,687,939**	530,969
	31,350,727	28,178,720
Other deductions:		
Interest on long-term debt	**2,456,714**	864,428
Miscellaneous	**1,404,337**	396,756
	3,861,051	1,261,184
INCOME BEFORE INCOME TAXES AND EXTRAORDINARY ITEMS	**27,489,676**	26,917,536
Income taxes:		
Federal	**13,649,000**	13,300,000
State	**872,000**	738,000
	14,521,000	14,038,000
INCOME BEFORE EXTRAORDINARY ITEMS	**12,968,676**	12,879,536
Extraordinary items — Note B:		
Additional monthly franchise fee income arising from change to accrual method of accounting, less related income taxes of $623,000	**552,285**	—
Provision for settlement of employment contracts, less related income taxes of $303,000—(deduction)	**(269,000)**	—
	283,285	—
NET INCOME	**$ 13,251,961**	$ 12,879,536
Per common share—Note I:		
Income before extraordinary items	**$1.24**	$1.24
Extraordinary items	**.03**	—
Net income	**$1.27**	$1.24

See notes to consolidated financial statements.

CONSOLIDATED BALANCE SHEET

Kentucky Fried Chicken Corporation
and Consolidated Subsidiaries

	September 30 1970	September 30 1969
ASSETS		
Current Assets		
Cash	**$ 16,462,827**	$ 10,416,754
Marketable securities — at cost (approximate market)	—	1,590,577
Notes and accounts receivable, less allowance for losses (1970—$720,269 and 1969—$371,224)	**16,752,752**	16,282,614
Amounts receivable for land, buildings, and store equipment sold—Note E	**8,402,821**	—
Merchandise inventory—at lower of cost (first-in, first-out method) or market	**9,053,852**	6,053,217
Prepayments and other current assets	**3,589,912**	1,319,937
TOTAL CURRENT ASSETS	**54,262,164**	35,663,099
Other Assets		
Equipment notes and contracts receivable for equipment rental, less unearned income (1970—$294,650 and 1969—$925,779)—Note E	**871,001**	3,539,098
Less amount due within one year included under current assets	**289,792**	1,585,758
	581,209	1,953,340
Investments in and advances to unconsolidated subsidiaries—Note A	**1,032,498**	—
Sundry other assets	**2,753,637**	2,019,348
	4,367,344	3,972,688
Property and Equipment — at cost, less allowance for depreciation and amortization — Notes C, D, and E	**75,314,434**	40,879,189
Intangible Assets		
Franchises and other intangible assets—at cost, less amortization—Note C	**1,267,695**	1,310,401
Cost in excess of net assets of consolidated subsidiaries at dates of acquisition—Note A	**11,901,911**	8,843,228
	13,169,606	10,153,629
	$147,113,548	$ 90,668,605

See notes to consolidated financial statements.

	September 30	
	1970	1969—Note A
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current Liabilities		
Notes payable — banks	**$ 11,360,018**	$ 556,635
Trade accounts payable	**12,228,825**	10,853,104
Deposits on franchise contracts	**1,653,469**	2,115,237
Accrued taxes and interest	**1,734,559**	1,244,273
Accrued compensation and related items	**1,694,390**	1,320,709
Federal and state income taxes	**9,858,100**	8,817,891
Dividends payable	**521,903**	323,427
Portion of long-term debt due within one year	**7,503,431**	2,170,745
TOTAL CURRENT LIABILITIES	**46,554,695**	27,402,021
Long-Term Debt—Note D	**40,480,853**	18,067,095
Other Long-Term Liability—Note B	**940,400**	—
Deferred Income—Note H	**1,108,099**	—
Shareholders' Equity—Notes A and G		
Preferred Stock—$100 par value: Authorized 500,000 shares; none issued	—	—
Common Stock—$1 par value: Authorized—30,000,000 shares Issued—10,541,205 shares in 1970; 10,444,439 shares in 1969 (including 185,350 shares in 1970 and 189,308 shares in 1969 in treasury)	**10,541,205**	10,444,439
Additional paid-in capital	**12,979,701**	12,678,663
Retained earnings	**34,894,651**	22,445,278
	58,415,557	45,568,380
Less cost of Common Stock in treasury	**386,056**	368,891
	58,029,501	45,199,489
COMMITMENTS AND CONTINGENT LIABILITIES—Note E		
	$147,113,548	$ 90,668,605

See notes to consolidated financial statements.

STATEMENT OF CONSOLIDATED SHAREHOLDERS' EQUITY

Kentucky Fried Chicken Corporation
and Consolidated Subsidiaries

	Common Stock $1 Par Value	Additional Paid-in Capital	Retained Earnings	Common Stock in Treasury
Balance at October 1, 1968	$ 9,667,340	$10,915,657	$ 9,845,258	$ (400,999)
Elimination of minority interest in Kentucky corporation	635,710	389,709	739,035	—
BALANCE AT OCTOBER 1, 1968, as restated	10,303,050	11,305,366	10,584,293	(400,999)
Stock options exercised	139,900	1,146,179	—	29,265
Preferred stock converted	1,489	—	—	—
Difference between capital of pooled companies acquired and par value of Common Stock issued in poolings of interests and related expenses and adjustments	—	79,664	17,001	—
Contribution to capital by former owner of pooled companies	—	85,664	—	—
Proceeds over cost of Common Stock acquired and sold by consolidated subsidiary	—	53,862	—	2,843
Miscellaneous	—	7,928	—	—
Net income for the year	—	—	12,879,536	—
Cash dividends declared—$0.10	—	—	(941,609)	—
Dividends and other adjustments of pooled companies prior to merger	—	—	(93,943)	—
BALANCE AT SEPTEMBER 30, 1969	10,444,439	12,678,663	22,445,278	(368,891)
Companies pooled during year—not restated for prior years	89,115	84,780	506,814	(25,693)
Stock options exercised	12,400	262,200	—	—
Proceeds over cost of Common Stock acquired and sold by consolidated subsidiaries	—	180,611	—	8,528
Adjustments of shares issued in prior poolings	(4,749)	4,749	—	—
Net income for the year	—	—	13,251,961	—
Cash dividends declared—$0.125	—	—	(1,302,340)	—
Adjustment to conform fiscal year of pooled company and other pooling adjustments and related expenses	—	(231,302)	(7,062)	—
BALANCE AT SEPTEMBER 30, 1970	$10,541,205	$12,979,701	$34,894,651	$ (386,056)

See notes to consolidated financial statements.

STATEMENT OF CONSOLIDATED SOURCE AND APPLICATION OF FUNDS

Kentucky Fried Chicken Corporation
and Consolidated Subsidiaries

	Year Ended September 30	
	1970	1969
Source of Funds		
Net income (after extraordinary items in 1970)	**$13,251,961**	$12,879,536
Depreciation and amortization	**5,034,924**	3,133,860
Provision for settlement of employment contracts—net (long-term portion)	**512,000**	—
FROM OPERATIONS	**18,798,885**	16,013,396
Proceeds from long-term loans from banks	**19,744,041**	13,601,584
Decrease in equipment notes and contracts receivable for equipment rental	**1,372,132**	—
Cash proceeds from exercise of stock options by employees and franchisees	**274,600**	715,344
Proceeds from sale of land, buildings, and store and transportation equipment	**12,172,498**	—
Other	**572,115**	355,976
TOTAL SOURCE OF FUNDS	**52,934,271**	30,686,300
Application of Funds		
Property and equipment—net	**48,302,132**	21,833,485
Cash dividends	**1,302,340**	979,349
Cost in excess of net assets of consolidated subsidiaries at dates of acquisition, less long-term debt incurred	**2,033,603**	3,493,635
Investments in and advances to unconsolidated subsidiaries	**1,032,498**	—
Other	**817,307**	1,763,568
TOTAL APPLICATION OF FUNDS	**53,487,880**	28,070,037
Increase (decrease) in working capital	**(553,609)**	2,616,263
Working capital at beginning of year	**8,261,078**	5,644,815
WORKING CAPITAL AT END OF YEAR	**$ 7,707,469**	$ 8,261,078

See notes to consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Kentucky Fried Chicken Corporation and Consolidated Subsidiaries

September 30, 1970

Note A—Principles of Consolidation, Liquidation of Kentucky Corporation and Acquisitions

The consolidated financial statements include the accounts of Kentucky Fried Chicken Corporation, a Delaware corporation ("KFC"), and its wholly-owned domestic and foreign subsidiaries. Intercompany accounts, transactions, and profits have been eliminated upon consolidation. Investments (all made in fiscal 1970) in unconsolidated majority-owned and 50% owned companies, and joint ventures are carried at cost adjusted for undistributed net earnings or losses since date of acquisition.

In July, 1970, after approval by the shareholders of Kentucky Fried Chicken Corporation (the Kentucky corporation), the parent Delaware corporation (KFC) consummated the plan of reorganization and dissolution of the Kentucky corporation initiated by the Exchange Offer made on May 5, 1969. Since at September 30, 1969, approximately 93% of the Kentucky corporation shares had been exchanged for KFC Common Stock, the then minority interest was segregated in the consolidated financial statements. In the accompanying financial statements, the 1969 statements have been restated to reflect the subsequent consummation of the reorganization and the elimination of the minority interest.

During the year ended September 30, 1970, KFC consummated five acquisitions accounted for as poolings of interests and the accounts and operations of the pooled companies are included for the entire current year. KFC also consummated 16 other acquisitions (exclusive of the acquisitions from Food Baron Corporation described later) representing purchase transactions and the operations of the purchased companies have been included herein since the respective dates of acquisition. The purchased businesses were acquired for cash and notes aggregating $3,991,385 (exclusive of obligations amounting to $1,415,241 assumed in the acquisitions). In connection with pooled acquisitions, 89,115 shares of Common Stock were issued, including 24,000 shares applicable to a group of companies acquired in October, 1970, under which up to 16,000 additional shares (maximum) may be issued contingent upon the future market price of KFC Common Stock. The 1969 consolidated financial statements have not been restated for the 1970 pooled companies since the effect on the consolidated financial statements would not be material.

Under agreement dated June 23, 1970, KFC purchased from Food Baron Corporation: (1) its roast beef operations and related assets, (2) franchise rights granted to them by KFC, and (3) the remaining 50% interest in two joint ventures, Kentucky Baron of California, Inc. and Kentucky Baron of Florida, Inc. Food Baron was required under the agreement to contribute to the capital of the roast beef subsidiaries all of the debts owed to it by such subsidiaries as of April 30, 1970, which aggregated at least $1,301,122. KFC was required to pay Food Baron $500,000 in cash on October 1, 1970, and $425,000 each on April 1, 1971 and October 1, 1971 in cash, notes, or Common Stock (at KFC's option). A $510,000 note due October 1, 1973, with interest at 8% was substituted for the cash payment due October 1, 1970, which Food Baron discounted at a bank. KFC agreed to repurchase the note any time at the bank's request after November 1, 1971 for $500,000. KFC entered into an employment and bonus arrangement dated June 23, 1970, with certain key officers and employees (see Note E).

The excess of cost of investment in subsidiaries acquired in purchase transactions over the net assets of such subsidiaries at dates of acquisition aggregated $11,901,911 at September 30, 1970, which amount is not being amortized since it is believed to be of continuing value.

Note B—Extraordinary Items

To be consistent with accrual accounting, KFC changed its method of accounting for monthly franchise fee income from the cash to the accrual basis beginning October 1, 1969. (Monthly franchise fees are based on current monthly sales of the franchisee and are distinct from initial franchise fees which are recognized in income when the outlet is opened.) With the expansion of its computer capabilities in fiscal 1970, KFC has been able to determine

NOTE B (continued)

monthly franchise fees more timely and was able to adopt the accrual method. This change resulted in an increase of approximately $600,000 in monthly franchise fees for the year ended September 30, 1970, or $300,000 in net income ($0.03 per share). Monthly franchise fees accrued at October 1, 1969, amounting to $1,175,285 ($552,285 net-of-tax) are reflected in this year's net income as an extraordinary credit.

Implementing the decision in 1969 to enter the motor hotel business, KFC employed two executives with considerable experience in the field, under a contract providing for a 5% stock interest in the motel subsidiary and a salary and bonus arrangement based on earnings of the motel subsidiary. KFC also agreed to contribute up to $15,000,000 in cash and stock to equity capital for the program. In connection with new financial arrangements with a group of banks completed in April, 1970, KFC was requested to substantially reduce its commitment. Accordingly, in September, 1970, KFC executed a termination and release agreement with these executives providing for payments over a period of 17 years in consideration of their releasing KFC from all its commitments to them. The estimated present value of these payments is $572,000. This amount (net-of-taxes) has been set forth as an extraordinary charge to income for the year.

Note C—Property and Equipment

Details of property and equipment are as follows:

	September 30 1970	September 30 1969
Buildings and improvements	$18,894,726	$ 7,840,004
Transportation equipment	1,311,569	2,452,604
Office furniture and equipment	2,312,611	580,095
Other equipment	24,056,657	17,779,710
Leasehold improvements, including retail outlets	20,705,171	8,861,228
	67,280,734	37,513,641
Less allowance for depreciation and amortization	11,102,043	7,374,353
	56,178,691	30,139,288
Land	15,944,756	8,617,746
Construction in progress (estimated cost to complete at September 30, 1970—$3,000,000)	3,190,987	2,122,155
TOTAL PROPERTY AND EQUIPMENT (see Note E)	$75,314,434	$40,879,189

Provision for depreciation of property and equipment amounted to $4,753,327 for the fiscal year 1970 and $2,849,459 for the fiscal year 1969 and has been made on a basis considered adequate to amortize the cost of depreciable assets over their estimated useful lives, generally by the straight-line method. The annual amounts of such allowances were computed on the basis of the following range of lives:

Buildings	10 to 40 years
Transportation equipment	3 to 8 years
Office furniture and equipment	3 to 10 years
Other equipment	3 to 10 years
Leasehold improvements	4 to 30 years

The cost of franchises, trademarks, and organization expenses are being amortized over periods of 60 to 210 months from date acquired or incurred. Amortization of intangibles amounted to $281,597 for 1970 and $278,385 for 1969.

Note D—Long-Term Debt

The details of long-term debt are as follows:

	September 30 1970	September 30 1969
Notes payable to banks due on various dates including interest primarily from 6% to 8% per annum	$31,974,000	$14,747,113
Mortgage notes payable in various installments including interest primarily from 6% to 9% per annum	10,778,200	2,596,859
Other installment notes due on various dates including interest primarily from 6% to 9% per annum	3,735,084	2,793,868
Other long-term obligations	1,497,000	100,000
	47,984,284	20,237,840
Less amounts due within one year included with current liabilities	7,503,431	2,170,745
TOTAL LONG-TERM DEBT	$40,480,853	$18,067,095

The mortgage notes payable are collateralized by deeds of trust, leasehold improvements, buildings, equipment, and other assets with a net carrying amount of approximately $16,024,000 and $4,350,000 at September 30, 1970 and September 30, 1969, respectively.

On April 30, 1970, KFC entered into an arrangement with a group of banks to provide an aggregate of $50,000,000 of long and short-term debt. The long-term portion consists of $30,000,000 (with interest payable quarterly at ½ of 1% over prime rate), representing revolving credit loans aggregating $15,000,000 maturing April 30, 1973 and $15,000,000 term loans payable in three equal annual installments due on April 30, 1971 through 1973.

KFC has prepayment privileges applicable to the long-term notes and is required to prepay the term loan notes from the net proceeds received from any sale and leaseback of land and buildings existing at April 30, 1970.

Under the terms of the loan and credit agreement, KFC is required to maintain consolidated working capital of $1,000,000 prior to October 1, 1970, $7,500,000 until July 1, 1971 (by waiver), and $10,000,000 thereafter. KFC may borrow short-term funds provided it is free of all such borrowings for sixty consecutive days in each twelve-month period after October 31, 1970. In addition, it may incur mortgage debt under certain circumstances and other long-term debt subordinated to the notes issued under this agreement, provided that the consolidated long-term senior indebtedness does not exceed 80% of consolidated tangible net worth. KFC may pay dividends or acquire any of its capital stock to the extent of 25% of its consolidated net earnings subsequent to September 30, 1969, plus $1,000,000 (retained earnings of $3,010,650 were available for such purposes at September 30, 1970). Other covenants limit guarantees of obligations, endorsements, loans, advances and similar matters by KFC.

A summary of the aggregate maturities of the long-term debt outstanding at September 30, 1970 follows:

Year ending September 30:	
1971	$ 7,503,431
1972	12,147,595
1973	20,947,440
1974	916,035
1975	852,250
Maturing beyond five years	5,617,533
	$47,984,284

Note E—Commitments for Financing, Leases, and Contingent Liabilities

In 1969, KFC sold real estate, on which its new corporate offices and motel are located in Louisville, Kentucky, to an insurance company for $700,000 and leased the land back under a lease dated November 18, 1969, providing for an initial term of 30 years at a basic annual rental of $73,220, plus additional rentals based on gross income of the motel and sublessees. The term may be extended for 69 years at a basic annual rental of 8% of the appraised value of the land plus the additional rentals. The leasehold estate cannot be encumbered in excess of 80% of the fair market value thereof. Under commitment letters dated September 3, 1969 with the insurance company and construction loan agreements dated November 18, 1969 with a bank, KFC borrowed $2,120,000 for the office building and Commenco Corporation (a subsidiary) borrowed $2,000,000 for the motel which buildings were to be erected on the land sold as described above. The loan for the office building (completed in 1970), financed by the insurance company, is secured by a first mortgage on the leasehold interests of KFC and is payable in equal monthly installments to July 15, 1996 (see Note D). The motel is expected to be completed in early 1971. Commenco has pledged its leasehold interests in the motel to a bank under a mortgage note dated September 30, 1970 to secure the loan for the motel. The note is due November 1, 1971 (see Note D).

In September, 1970, KFC and certain subsidiaries sold certain land and buildings ($4,055,657) and store equipment ($7,969,164) at the net carrying value on the books of the respective corporation (tax basis) under various agreements providing for lease back of such properties to KFC and its subsidiaries. At September 30, 1970, KFC had received $3,401,894 in cash from one institution and the balance after deduction for security deposits ($220,106) is due from six financial institutions together with a six-month note for $847,011 receivable from an individual purchaser. The leases of land and buildings are for terms of 20 years with renewal and purchase options. The leases covering store equipment are for various periods from five to eight years with certain purchase options or requirements at the end of the lease term.

KFC and its subsidiaries were lessees at September 30, 1970 under 750 leases having terms expiring from 1970 to 1999. The leases call for minimum rentals, exclusive of real estate taxes, maintenance and insurance payments required by some leases. Aggregate minimum rentals (exclusive of payments for expenses) for the periods ending September 30 are as follows:

1971-1975	$45,485,337
1976-1980	28,053,801
1981-1985	19,195,310
1986-1990	11,743,235
1991 and subsequent	2,208,643

Under an employment and bonus arrangement dated June 23, 1970 (date of the purchase agreement described in Note A), KFC agreed to offer employment to five officers of Food Baron Corporation. The principal officer is to receive a salary of not less than $36,000 per year for three years and has operating responsibility for certain roast beef operations. The bonus arrangement provides for payment to the five officers in cash of 10% of consolidated net profit before taxes (as defined in the agreement) of certain roast beef and fish operations for each fiscal year up to an aggregate maximum bonus of $800,000. The bonus arrangement will cease with termination of employment of the principal officer and, if his employment is terminated by death or he is discharged without cause, the bonus arrangement will terminate three years thereafter.

At September 30, 1970, KFC and its subsidiary had a contingent liability for equipment notes and contracts receivable discounted to banks amounting to $4,805,554.

NOTE E (continued)

KFC and certain subsidiaries entered into an agreement in 1970 with a leasing firm to purchase certain automatic chicken cookers from KFC's manufacturing subsidiary and to lease the cookers back to another KFC subsidiary which in turn leases such cookers to franchisees and KFC owned and operated outlets. The leasing firm is required to purchase up to $6,000,000 of cookers in one year. The KFC leasing subsidiary has certain purchase or renewal options at the end of the lease term. Sales of cookers under the agreement aggregated approximately $3,400,000 during fiscal 1970.

Note F—Profit Sharing Plan

Effective September 30, 1970, KFC amended its contributory profit sharing plan by termination of contributions to the Plan by KFC and by the employee-participants. Subject to receipt of a favorable ruling from Internal Revenue Service, the benefits for each participant in the Plan will become fully vested and the Plan will then be dissolved. The amounts charged against income were $93,757 and $82,780 for fiscal 1970 and 1969, respectively.

Management is considering the adoption of a new pension plan. However, at the date of this report, no specific plan had been consummated.

Note G—Stock Options and Other Reserved Shares

Qualified Stock Options:

Under the 1970 Qualified Stock Option Plan (approved by the Shareholders on February 10, 1970), 150,000 shares of KFC's Common Stock were reserved for issuance under options which may be granted to officers and other employees. The option price cannot be less than 100% of fair market value at the time the option is granted and is payable in full in cash upon exercise of option. Options may be granted under the Plan until December 22, 1979, and are exercisable over a period commencing one year, but not exceeding five years, from the respective dates the options are granted. The stock subject to these options may be purchased one-third each year on a cumulative basis. Options had been granted under prior plans with provisions that do not differ significantly from the above, but authority to grant options under those plans had been terminated prior to September 30, 1970.

At October 1, 1969, there were options outstanding to purchase 109,125 shares of Common Stock at prices ranging from $11.29 to $53.00 per share (aggregate option price—$4,428,848). During the year, options were granted for 120,400 shares at prices ranging from $14.375 to $54.25 per share (aggregate option price—$3,849,237). Options were exercised for 12,400 shares at prices ranging from $11.29 to $39.38 (aggregate option price—$274,600) and options for 69,400 shares were terminated without being exercised. At September 30, 1970, there were options outstanding for 147,725 shares (41,425 shares exercisable) at prices ranging from $14.375 to $53.00 (aggregate option price—$5,106,455) with 76,700 shares reserved for future options.

NOTE G (continued)

Other Stock Options:

On June 9, 1969, the Executive Committee of the Board adopted a Restricted Stock Purchase Plan reserving 150,000 (restricted to 50,000 under the Loan and Credit Agreement dated April 30, 1970) shares of KFC's Common Stock for future offer and sale to key executives of KFC (approved by Shareholders on February 10, 1970). Under the terms of the Plan, shares may be sold to eligible executives at a purchase price equal to 66⅔% of the fair market value on the date the offer is approved. The full purchase price must be paid within 60 days of the offer, but KFC may loan an executive up to 100% of the purchase price subject to certain terms and conditions including the receipt of the executive's promissory note with full personal liability, interest at not less than 4% per annum and secured by pledge of the shares purchased. There are also certain restrictions on sale or other disposition of the shares purchased under the Plan. At September 30, 1970, no shares have been offered or purchased under this Plan.

At September 30, 1970, KFC was holding non-recourse, non-interest bearing promissory notes due January 15, 1974, aggregating $600,000, which it received from three directors in payment for 15,000 shares of KFC Common Stock under stock options exercised in July, 1969. The stock is held as collateral for the notes.

Colonel Sanders' Inns, Inc. (CSI), a subsidiary of KFC, has granted an option to Colonel Harland Sanders to purchase 10,000 shares of CSI Common Stock at the time of a public offering, if any, of CSI stock in exchange for the right to use the name and likeness of Colonel Sanders in connection with motels that CSI is to own or franchise. KFC has agreed to loan Colonel Sanders the purchase price of this option, interest free, for five years.

Other Reserved Shares:

Under contingent payout provisions of acquisition agreements for two pooled companies, KFC may be required to issue up to 160,500 additional shares contingent upon future earnings and market prices.

Note H—Deferred Income

It is the accounting practice of KFC to eliminate upon consolidation any intercompany profit in equipment sold between its affiliated corporations. However, gain arising from equipment sold under sale and leaseback agreements (described in Note E), which would otherwise be recognized upon sale of equipment to parties outside the consolidated group, has been deferred and is being amortized over the term of the related leases.

Note I—Income Per Share

Net income per share for fiscal 1970 has been based upon the average number of shares of Common Stock outstanding for the year which average number has been increased by additional shares that could be issued (based upon current conditions) under contingent payout provisions of agreements for pooled companies. Stock options are not dilutive in 1970. Net income per share for fiscal 1969 has been restated to reflect the additional shares issued or contingently issuable based on current conditions.

Accountants' Report

Board of Directors and Shareholders
Kentucky Fried Chicken Corporation
Louisville, Kentucky

We have examined the consolidated balance sheet of Kentucky Fried Chicken Corporation and consolidated subsidiaries as of September 30, 1970, and the related statements of consolidated operations, shareholders' equity, and source and application of funds for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances. We previously made an examination of the consolidated financial statements for the preceding year.

In our opinion, the accompanying balance sheet and statements of operations, shareholders' equity, and source and application of funds present fairly the consolidated financial position of Kentucky Fried Chicken Corporation and consolidated subsidiaries at September 30, 1970, and the consolidated results of their operations, changes in shareholders' equity, and the source and application of funds for the year then ended, in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year, except for the change (in which we concur) in accounting for monthly franchise fees as described in Note B.

Ernst & Ernst

Louisville, Kentucky
December 21, 1970

Directors

John Y. Brown, Jr.
President, Chairman of the Board and Chief Executive Officer

Richard C. Beeson
Executive Vice President, Chief Operating Officer

Sam Fleming
President, Third National Bank in Nashville
Nashville, Tennessee

J. David Grissom
Executive Vice President, Extendicare Inc.;
Partner, Greenebaum Grissom Doll Matthews & Boone
Louisville, Kentucky

Ervin E. Hanks
President, Speck Enterprises, Inc.
Portland, Oregon
(deceased, October 23, 1970)

Leon W. Harman
President, Quality Distributors, Inc.
Los Altos, California

Joseph I. Kesselman
Group Vice President, Finance and Administration

John M. Mihalic, Jr.
Group Vice President, Avco Corporation

Haddon Salt, esq.
Goodwill Ambassador

Elvis Stahr
President, National Audubon Society

William T. Young
Board Chairman, Royal Crown Cola Co.

Director Emeritus

Colonel Harland Sanders
Goodwill Ambassador

Officers

John Y. Brown, Jr.
President, Chairman of the Board and Chief Executive Officer

Richard C. Beeson
Executive Vice President, Chief Operating Officer

Robert S. Barlow
Group Vice President, Operations

Joseph I. Kesselman
Group Vice President, Finance and Administration

Robert Lapointe
Senior Vice President, International

Ted P. Cullin
Vice President, Franchisee Relations

Peter B. Curlin
Vice President, Financial Planning

William B. Evans
Vice President, Operations

Patrick H. Gorman
Vice President, Marketing and Advertising

Norman N. Habermann
Vice President, Franchising

Richard McFarland
Vice President, Purchasing

Arthur F. Pelster
Vice President, Research & Development

Kenneth B. Wolfe
Vice President, Organizational Development

Charles G. Hitner
Treasurer

Edward E. Ellis
General Counsel and Secretary

Transfer Agents

Third National Bank in Nashville
Nashville, Tennessee

First National City Bank
New York City

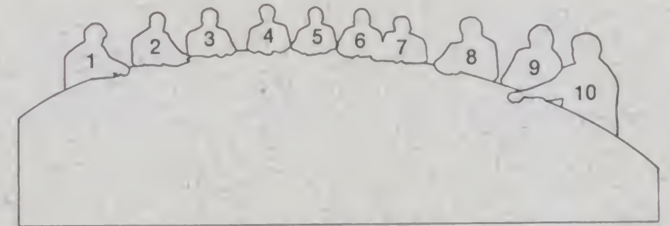
Registrars

First American National Bank
Nashville, Tennessee

Bankers Trust Company
New York City

Auditors

Ernst & Ernst



Board of Directors: 1. Haddon Salt, esq.; 2. Sam Fleming; 3. J. David Grissom; 4. Leon W. Harman; 5. John Y. Brown, Jr.; 6. John M. Mihalic, Jr.; 7. Joseph I. Kesselman; 8. Ervin E. Hanks, (deceased); 9. Richard C. Beeson; 10. Elvis Stahr. Not Pictured: William T. Young.

Alan F. Frank, left, chairman of the KFC National Advertising Cooperative Committee, confers with Patrick Gorman, seated, KFC vice president, marketing and advertising; and David S. Mathewson, executive secretary of the co-op program.

ADVERTISING AND PROMOTION

Colonel Harland Sanders, the founder of Kentucky Fried Chicken, and Haddon Salt, the founder of H. Salt, esq., English Fish & Chips, remain the only authentic food experts who have become personalities within an industry which has built its promotional appeal around personalities. Both have developed convenient food products of distinctive taste and quality, and both radiate a personal charm that enhances their many appearances on behalf of Kentucky Fried Chicken Corporation and its franchisees.

More consumers than ever before were reached by, and responded to, the 1970 national advertising campaign which was the most comprehensive in the food service industry. This campaign, supported by a National Cooperative Advertising Program budget of more than $5 million, was the largest single portion of an extensive promotional program which included newspaper and magazine advertisements, local and national radio and television commercials, outdoor advertising, point-of-sale promotions and both personal and nationally televised guest celebrity appearances by Colonel Sanders and Haddon Salt. The Colonel's 80th birthday at the close of fiscal 1970 was the focal point of the Company's largest single nationwide promotion.

The KFC National Cooperative advertising budget, which represents approximately 20 per cent of the combined promotional expenditures of the Company and its franchisees,

is funded by appropriations from franchised and Company-owned outlets and additional Company allocations. Its staff administers the program under the direction of a committee composed of franchisees and Company representatives.

A field marketing division has been established to counsel field managers, local advertising groups and franchisees on more effective use of their local advertising budgets based upon successful field-tested advertising promotional campaigns. As part of this program, regional marketing managers supervise studies intended to tailor promotional efforts to specific stores, markets and regions.

Data gathered in an extensive consumer survey conducted in 1970 will serve as an important tool in the development of an even more effective overall advertising program for 1971. This survey projected a specific consumer profile, determined purchasing habits and motivations, and provided a variety of information for a more selective advertising approach.

H. Salt, esq., English Fish & Chips advertising, which is being patterned after the successful Kentucky Fried Chicken program, reached consumers through franchisees on a local basis during 1970.

Kentucky Fried Chicken Corporation, which pioneered the national advertising cooperative concept in the food service industry, is preparing a 1971 advertising and promotion program which will be the most extensive in the Company's history.

Colonel Sanders cuts a slice of cake for KFC President John Y. Brown, Jr. during an 80th birthday party attended by 1,200 persons, including franchisees and such dignitaries as Norman Vincent Peale and Kentucky Governor Louie B. Nunn.

Product research was augmented in 1970 by completion of this new corporate test kitchen, equipped with the company's automatic cooker, in background.

RESEARCH AND DEVELOPMENT

Quality control, cost reduction and increased unit sales volume through new products were the primary targets of Company research and development activity during fiscal 1970.

The year will be remembered as the year of the automatic cooker in the kitchens of hundreds of Kentucky Fried Chicken outlets, where this product of past research and development went into operation for the first time. The automatic cooker is capable of simultaneously preparing 180 pieces of chicken to exacting quality standards.

The Company anticipates further breakthroughs from the same research and development which produced this industry innovation, and is emphasizing the program both at KFC Manufacturing in Nashville, where the cooker is assembled, and in the fully equipped new test kitchen in Louisville, where new products are being developed.

Product research is directly coordinated with market research, through which consumer buying patterns and the prospective acceptance of new products are studied. During 1970, this coordinated effort resulted in the introduction of a broader menu at H. Salt, esq., English Fish & Chips outlets, the expansion of menu selection at Kentucky Fried Chicken outlets and the development of a new concept at some Kentucky Roast Beef locations.

Kentucky Fried Chicken Corporation's growth during the 1960s resulted from the combination of expansion in new market areas and increased sales volume in existing outlets. The introduction of new products intended to increase unit volume is a key objective for 1971.

Building design modifications for maximum economy and efficiency are a major research and development project. This one features a common dining area between two franchised outlets.

Kentucky Fried Chicken Corporation counts among its greatest assets a distinctive building with which consumers automatically identify, and products of high quality and unduplicated taste which are equally appropriate in the picnic basket and on the festive dinner table.

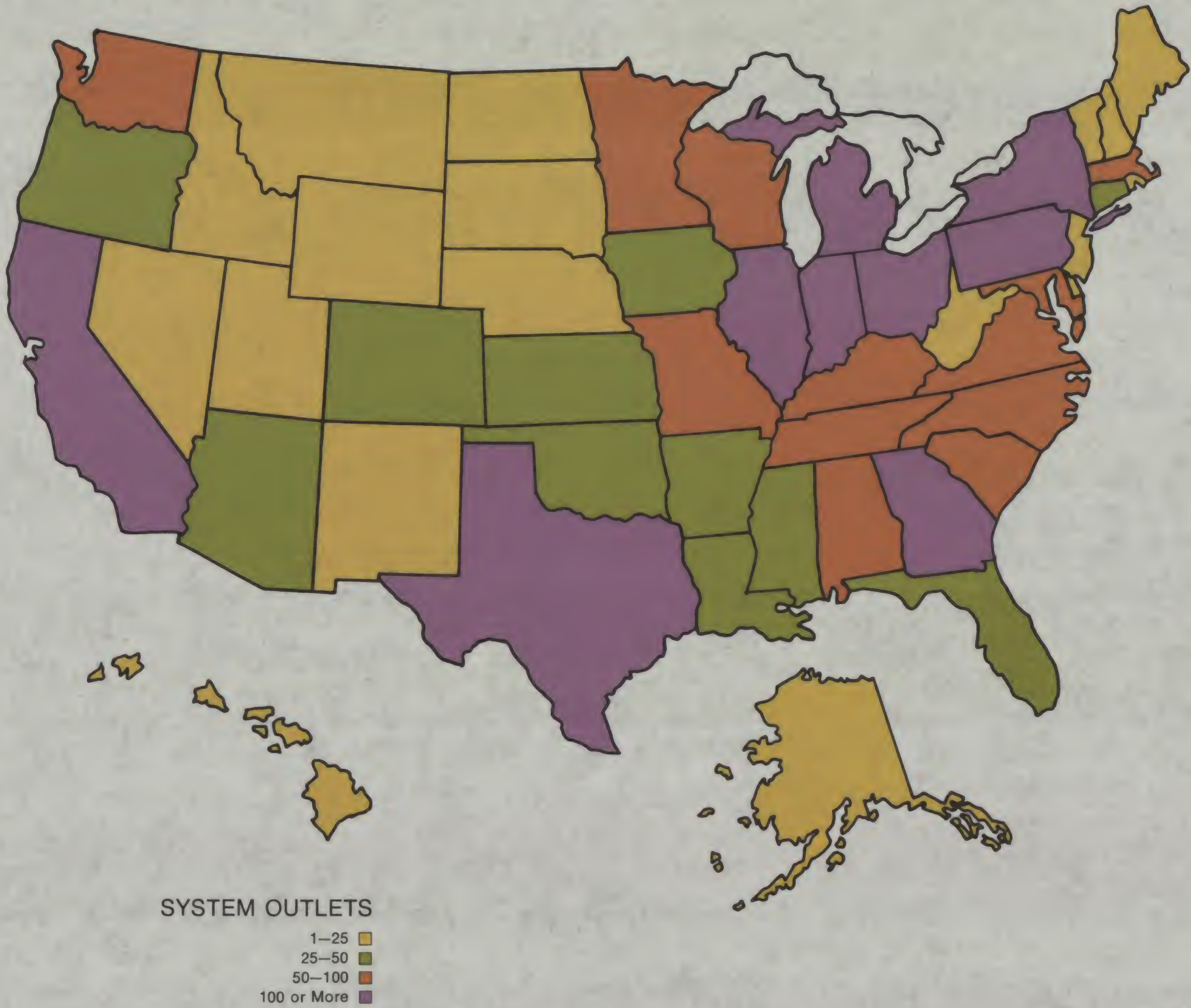
KFC INTERNATIONAL

International consumer acceptance of Kentucky Fried Chicken and H. Salt, esq., English Fish & Chips in new markets continued to underline the future significance of this unparalleled long-range market opportunity during fiscal 1970. With the opening of 109 new units during the year, the products of Kentucky Fried Chicken Corporation now are available through 170 units in 22 markets outside the United States.

Australia continues to provide a dramatic advance profile of expansion potential for Kentucky Fried Chicken in the international market. Established just three years ago, the Australian operation now has 30 Company-owned and 38 franchised stores, with average unit sales volume higher than that of the domestic market. Consumer acceptance during 1970 in test situations in Japan was particularly encouraging. A Kentucky Fried Chicken store located at Expo '70 in Osaka was one of the Company's greatest sales volume leaders.

Extensive investment in the European market, which has not yet produced profits, opens an area which should provide considerable prospects for growth. The Company also has started development of the South American market. Each of these markets has its own peculiarities, requiring studies to determine the best system of distribution, service and profitability.

Establishing a position of international leadership similar to that enjoyed in the United States is a major corporate objective. Expansion of international operations will continue during 1971 within investment limitations imposed by the United States Government and within the restrictions of foreign governments. The international market is expected to contribute to profits on a significant basis within two years.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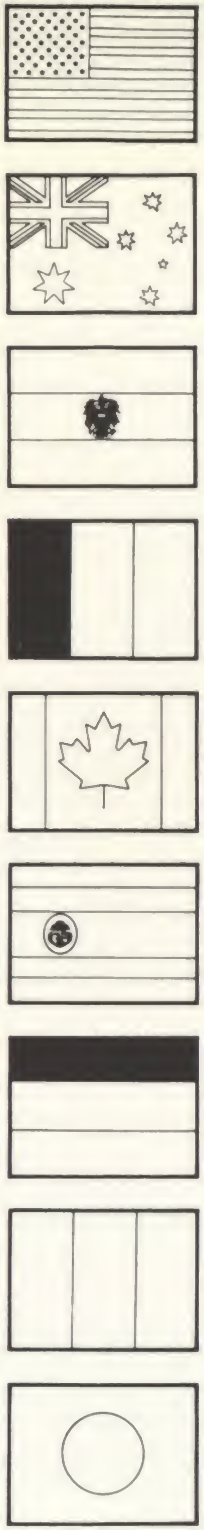
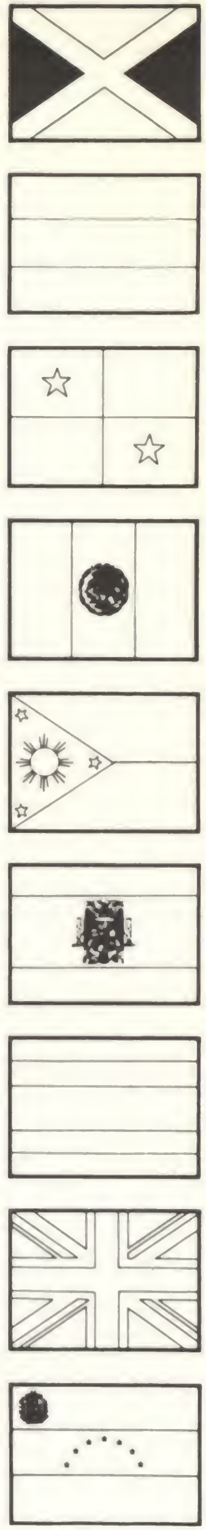



Kentucky Fried Chicken
TAKE HOME SERVICE
Kentucky Fried Chicken



Kentucky Fried Chicken Corporation
1441 Gardiner Lane
Louisville, Kentucky 40213